LOS ANGELES BAR BULLETIN

In This Issue

A Word From the President . . . *Alex W. Davis* 161

Committee on Lawyers Reference Service Gives 1946 Summary 162

The Mt. Clemens "Court To Court" Case . . . . . *William B. Carman, Jr.* 165

Legal Semantics . . . . . *Ewell D. Moore* 169

Federal Securities Act Exemptions and The General Practitioner . *Graham L. Sterling, Jr.* 172

Rule 14—Judicial Council 192

VOL. 22 FEBRUARY, 1947 NO. 6

LOS ANGELES
BAR BULLETIN

Official Monthly Publication of Los Angeles Bar Association. Entered as second class matter October 15, 1943, at the Postoffice at Los Angeles, California, under Act of March 3, 1879. Subscription Price $1.00 a Year; 10c a Copy.

VOL. 22 FEBRUARY, 1947 No. 6

BULLETIN BUSINESS OFFICE
241 East Fourth Street
TRinity 5206

BULLETIN EDITORIAL OFFICE
1124 Rowan Building
TUcker 8118

A WORD FROM THE PRESIDENT

IN retiring from office at the close of the Association year, I have sought to analyze the philosophy which inspires lawyers to belong to a bar association and to do the work required to keep it going. Following the practice of lawyers in relying on precedent or authority I have searched for authoritative statements of recognized philosophers. De Tocqueville expressed the thoughts which I have had in mind, crediting as accomplishments what I would classify as aims. He said:

"The special information which lawyers derive from their studies ensures them a separate station in society, and they constitute a sort of privileged body in the scale of intelligence. . . . they naturally constitute a body, not by any previous understanding or by an agreement, which directs them to a common end; but the analogy of their studies and the uniformity of their proceedings connect their minds together, as much as a common interest could combine their endeavors. . . . Lawyers belong to the people by birth and interest, to the aristocracy by habit and by taste, and they may be looked upon as the natural bond and connecting link of the two great classes of

society. . . . A privileged body can never satisfy the ambition of all its members; it has always more talents and more passions to content and to employ than it can find places; so that a considerable number of individuals are usually to be met with who are inclined to attack those very privileges which they find it impossible to turn to their own account. . . . The more we reflect upon all that occurs in the United States the more shall we be persuaded that the lawyers as a body form the most powerful, if not the only, counterpoise to the democratic element. In that country we perceive how eminently the legal profession is qualified by its powers, and even by its defects, to neutralize the vices which are inherent in popular government."

"The lawyers of the United States form a party which is but little feared and scarcely perceived, which has no badge peculiar to itself, which adapts itself with great flexibility to the exigencies of the time, and accommodates itself to all the movements of the social body; but this party extends over the whole community, and it penetrates into all classes of society; it acts upon the country imperceptibly, but it finally fashions it to suit its purposes."

It seems natural that lawyers should organize to maintain or acquire for themselves a position in society to justify these observations of a distinguished traveler and to make the most of their opportunities to promote the administration of justice and maintain the honor and dignity of the profession.

Alex W. Davis

COMMITTEE ON LAWYERS REFERENCE SERVICE GIVES 1946 SUMMARY

THE Los Angeles Bar Association Committee on Lawyers Reference Service, of which William Howard Nicholas is Chairman, has submitted to the Board of Trustees of the Association its annual report concerning the work of the 1946 Committee. In the December, 1946, issue of the BAR BULLETIN, Alex W. Davis, President of the Association, in his monthly article under the title "A Word from the President" stated,

"The lack of knowledge that a lawyer's services are needed can be cured only by continuing education. The Association for several months has engaged in a new experiment of direct education by conducting a radio program over Station KGFJ (1230) at 5:40 P. M. on Tuesday and Thursday. . . ." The annual report indicates that the Committee thoroughly agrees with Mr. Davis' views on this matter.

The Lawyers Reference Service Committee recommends that adequate publicity be given to the fact that the Service is available to the public on a minimum fee basis for the first consultation. The report states, "If we get our story across to the public by an appropriate advertising program, it will do much to offset the growing tendency of members of the lay public needing legal advice, getting such advice from real estate brokers, insurance brokers, bank clerks and managers, escrow officers, stock and bond brokers and a horde of other classes of gratuitous curbstone legal advisers . . . We feel that by such a program the Bar will do a public relations job and at the same time perform a better public service."

The Board of Trustees approved the Committee's recommendation that a portion of the funds now on hand in the Lawyers Reference Service Fund be used to publicize the Service. All registration fees paid by those in the Service are kept in a separate fund and used only in behalf of the Service.

Another recommendation of the Committee is that the names of three attorneys be given to the applicant—five are given at the present time. This recommendation was approved by the Board.

The report has appended to it statistical data concerning references made during the year. It is interesting to note that the service handled 1,606 cases, which is the largest number ever handled during a calendar year. There are 326 attorneys registered in the service. The results for the coming year should be even more encouraging.

Table I on the following page shows the references made according to the branch of law involved, and also the number of lawyer's cards on file for each subject or specialty. Table II covers special references where either foreign law or a knowledge of a foreign language is involved.

TABLE I

References by Branch of Law Involved

Branch of Law	References to Attorneys	References to Laymen	Total	Lawyers Cards on File
Administrative Law	4	62	66	48
Admiralty	2	8	10	4
Aliens	4	17	21	11
Appellate Practice	—	2	2	17
Bankruptcy	—	19	19	32
Copyright and Trademark	—	10	10	9
Condemnation Proceedings	—	—	—	14
Corporation Law	—	26	26	86
Criminal Law	—	54	54	56
Divorce	—	397	397	216
General Practice	1	316	317	21
Insurance	—	24	24	20
Labor Relations	1	5	6	24
Mechanics' Liens	—	—	—	9
Mining Law	11	11	22	9
Motion Picture	—	1	1	10
Oil and Gas	—	—	—	30
Patents	1	45	46	6
Personal Injury	4	104	108	159
Probate	—	81	81	252
Real Property	—	330	330	95
Taxation	1	7	8	47
Trusts	1	—	1	23
Water Rights	1	2	3	4
Workmen's Compensation	—	54	54	20
	31	1575	1606	

TABLE II

References Where Subject Matter Is to Law of Another Jurisdiction or Foreign Language Is Required

	References to Attorneys	References to Laymen	Total	Lawyers Cards on File
Arizona	—	11	11	2
Colorado	—	1	1	5
Florida	—	1	1	2
German	—	1	1	16
Hawaii	—	1	1	1
Illinois	1	1	2	6
Italian	—	2	2	3
Mexican	1	2	3	3
Nebraska	—	1	1	1
Nevada	—	2	2	1
New York	1	1	2	13
Oklahoma	—	2	2	5
Oregon	—	1	1	1
Pennsylvania	—	1	1	1
Texas	—	2	2	3
	3	30	33	

THE MT. CLEMENS "COURT TO COURT" CASE

By William B. Carman, Jr., of the Los Angeles Bar

LATE in 1945, the United States Supreme Court granted certiorari to a little group of seven employees of a moderately sized pottery plant in Michigan who had seen a judgment against their employer for a few thousand dollars reversed by the Circuit Court of Appeals. On the last decision-day of the 1945-46 term the high court reversed the decision and remanded the case for further proceedings. Nobody paid very much attention to this rather obscure lawsuit at the first. But within a few months of the decision, American industry awoke to find itself confronted with a myriad of claims, aggregating literally billions of dollars, and threatening either the bankruptcy of many large concerns or, in the alternative, a tremendous burden on the nation's taxpayers. The press was filled with reports of new "portal-to-portal" suits, labor organization representatives alternatively gloated or deplored, and a harassed Congress unwillingly faced a new, and to them a totally unnecessary, industrial problem. In the face of such furor the case itself deserves a brief discussion.

The Mt. Clemens Pottery Company at Mt. Clemens, Michigan, employs about 1200 workers. It operates with the same general procedures as do most industrial factories. That means a working day of eight hours, say from 7:00 to 12:00 noon and 1:00 to 4:00 in the afternoon. Employees are expected theoretically to be at their posts ready to work when the whistle blows at 7:00 and to stop work when the whistle blows at 4:00. They "clock in" at the factory entrance time-gate as much before starting time as they please, walk to their jobs, do such preliminary preparation as is necessary or as they think desirable, and are expected to be ready to work on the whistle. At night, they, again theoretically, quit work on the whistle, wash or change if desirable, "clock out" after walking to the gate, and go home. They are paid for the productive work they do from whistle to whistle. That is the standard pattern of most American industries, as old in many cases as the particular industry itself.

The Fair Labor Standards Act provides in effect that any employer under the scope of its provisions who employs "covered" employees for a work week longer than 40 hours must pay such employee at the rate of time and one-half for the hours in excess of 40, and that for failure so to do the employee may recover not only the deficit in wages, but an additional equal amount as "liquidated damages."[1] One Steve Anderson, six of his fellow employees, and their local C. I. O. union brought a representative action against their employer, the Mt. Clemens Pottery Company, in the Federal Court for the Eastern District of Michigan under these sections of the act. They alleged that the company required them to come to work fourteen minutes ahead of the whistle and to stay an equivalent time after the whistle, that they worked during such periods without pay, and hence were entitled to double the unpaid overtime. This the company denied.

The case was sent to a Master who found that the employer made no such requirement. He found further that though the employees came to the plant at varying times before the whistle, in order to get to their stations and get ready for work, they had not established by the preponderance of the evidence that they in fact worked before or after the whistle, and recommended dismissal. When the District Court reviewed his findings, it disagreed in part. Judge Frank Picard, to whom the case was assigned, believed that in fact the employees *did* go to work as soon as they got to their posts, even though that was before the whistle blew. He determined that the average time to "clock in," walk to work, and get ready was seven minutes. He, therefore, *deducted* seven minutes from the time shown on the time clock as walking and preparation time for which no compensation was to be paid and declared all other time compensable, with, of course, the statutory penalty when it ran over 40 hours per week. He thus definitely (and, in his opinion, specifically) *denied* any pay for walking or preparatory time.

On appeal by the Company the Circuit Court of Appeals reversed on the ground that the court erred in rejecting the Master's findings. Certiorari followed, and on June 10, 1946, the Supreme Court reversed the Circuit Court of Appeals.

---

[1]U. S. C., Title 29, §§207, 216.

The opinion was written by Mr. Justice Murphy. He agreed with the Circuit Court that the Master's finding of *fact* that the employees did not start productive work before the whistle must be sustained. But he found as a matter of *law* that walking time and preparation time was necessarily includable in the work week under the act. The gist of his opinion was as follows:

> "It follows that the time spent in walking to work on the employer's premises, after the time clocks were punched, involved 'physical or mental exertion (whether burdensome or not) controlled or required by the employer and pursued necessarily and primarily for the benefit of the employer and his business.' (*Tennessee Coal Co. v. Muscoda Local,* 321 U. S. 590, 598; *Jewell Ridge Co. v. Local No. 6167,* 325 U. S. 161, 164-166.) Work of that character must be included in the statutory work week and compensated accordingly, regardless of contrary custom or contract."

Thus for the first time in the case there was brought in an entirely new idea, the genesis of the "portal-to-portal" rule. The cases cited by the Justice were those involving the coal and iron miners,[2] in which the "travel time" counted was a matter not only of substance but of discomfort and danger, stressed highly by Justice Murphy in his opinion in those cases. The result of extending that principle to the *Mt. Clemens* case was to subject the nation's ordinary industries to the burden of paying retroactively *three times as much* for non-productive "walking" or "preparation" time as it was paying for actual work time, since the newly discovered portion of the work week had to be paid for at time and one-half plus the equivalent amount as a mandatory statutory penalty. And this in the face of generation-old custom and practice, embodied in many cases in collective bargaining contracts, as stressed in the dissent of Justices Burton and Frankfurter.

However, Mr. Justice Murphy held out one ray of hope to the employer—the rule *de minimis.* He said:

> "The work week . . . must be computed in light of the realities of the industrial world. When the matter in issue concerns only a few seconds or minutes of work be-

[2]Mr. Justice Jackson's vigorous dissent in the 5-4 decision in the *Jewell* case is worthy of careful reading.

> yond the scheduled working hours, such trifles may be disregarded. Split-second absurdities are not justified by the actualities of working conditions or by the policy of the Fair Labor Standards Act. It is only when an employee is required to give up a substantial measure of his time and effort that compensable working time is involved."

He remanded the case to the District Court to find what, if any, compensable time was due the plaintiffs.

Judge Picard, after a vehement and thoroughly understandable denial that *he* had anything to do with the abhorred "portal-to-portal" doctrine, set manfully to work to obey his mandate. He was met at the outset with a phenomenon not unfamiliar to practicing lawyers. Whereas in 1943 the employees' witnesses testified they reached their posts in less than two minutes, and immediately went to work, the testimony on their behalf now showed that any attempt to be ready for work in less than ten minutes was wholly beyond the realm of possibility. On the other hand, those same employees who by the employer's witnesses in 1943 needed vast quantities of time to get on the job now traveled, according to the same witnesses, with practically the speed of light. Nevertheless, Judge Picard persevered, and on February 8, 1947, came up with his solution. He found that the maximum walking time to the job was 6.2 minutes, that the walking time from the job or at lunch time was not to be considered as it was not for the employer's benefit, that the maximum preparation time was 2 minutes, and that as far as he was concerned the whole thing was *de minimis*. He also offered the suggestion that in no event should the Supreme Court's ruling be made effective for any periods prior to its date, June 10, 1946, a suggestion which, regardless of its practical merit, certainly will raise some legal eyebrows.

Judge Picard's decision is undoubtedly again on its way to the Supreme Court. It is, of course, only one opinion, and applicable to one single case. Nevertheless it is hoped that by this now famous "court to court" case, and possible Congressional action, the law on compensable working time will at last be clarified.[3]

---

[3]The *Mt. Clemens* case is reported *sub non Anderson v. Mt. Clemens Pottery Company* in 60 F. Supp. 146 (D. C. E. D. Mich., 1943); 149

LEGAL SEMANTICS

By Ewell D. Moore, of the Los Angeles Bar

IN order "to put the legal profession on a plain English basis," the head of an eastern Trust company urges lawyers to simplify their language. He is not concerned about the language of the court room, he says, but is much concerned with the language in wills, trust agreements and contracts.

This has long been an interesting subject of discussion, from time to time. Not that there is anything new or novel in the suggestion; but because, in these changing times it seems to deserve some notice by the bar, there is excuse for these comments. Like so many other suggestions offered by laymen to lawyers, it probably will lead to no practical results. Lawyers are wedded to "forms."

Few of those who "live by the law" ever cease to worship the written word as used over and over in our laws and law books. We anchor a word to a more or less lucid and typical example of its use, and thus allow words to control us, instead of making them our slaves. The same ideas in the same words, in the same places, make the language of the law and lawyers arid and boring.

It has been truly said that our language is never static; not even for a day. Perhaps we have not realized that truth; or, if we have, it may be that the language of the law is the exception. Some words are like old shoes; they are used for a while and then thrown away; others are held onto and put to new usages. Every lawyer should know too much to want to copy anyone. But one hesitates to venture the role of a "reformer"; especially if the custom is so firmly fixed as the use of legal terms and terminology. But it appears that lawyers never throw away any of the stilted phrases that became fixtures in the dim and distant past of law practice.

Since this is not intended to be a serious, big-word article, we shall confine our discussion to a few of the shortest, simplest words in the English language, such as "and," "or," and especially "and/or" so often used and misused in legal documents.

F. (2d) 461 (C. C. A. 6, 1945); 90 L. Ed. 1114 (U. S. S. C., 1946). The latest opinion of Judge Picard is as yet unreported. It is dated February 8, 1947. Plaintiff's complaint was dismissed February 13, 1947.

Don't think that because these are among the first to be lisped by infants they have escaped the serious attention of our courts. Many ponderous decisions are embalmed in the towers of tomes in our libraries wherein "and," "or," and "and/or" are expertly dissected, analyzed and defined, sometimes to the confusion of all parties concerned.

It would seem that anyone of jitterbug mentality knows the difference between "and" and "or," but don't be too sure. Many of our courts have said that "or" is often construed as "and," and vice versa. For example, one decision says: "The particle 'and' may be used to conjoin two coordinate phrases, whereas, in fact the thought in the second is subordinate to the first, so that the presence of 'and' conjoining coordinate phrases does not necessarily import more than one purpose."

Or, consider this weighty judicial pronouncement dealing with the use of the two little companions "and" and "or." "Each of the terms 'or' and 'and' has the meaning of the other or both when the subject matter, sense or connection requires such construction."

If you are not yet sufficiently confused, let us take up that strange mismated combination of "and" and "or" separated by an oblique line, namely, old friend "and/or." It has often met with rough treatment by the courts. One decision dealt out this verbal punch: "The symbol 'and/or' is not the English language within the terms of the constitutional provisions requiring that judicial proceedings be conducted and preserved in the English language." A less exacting judge let "and/or" get by with this comment: "The use of 'and/or' in legal documents, pleadings and statutes is subject to condemnation as being confusing and misleading."

One of our local judges, now deceased, was especially peeved to see "and/or" in so many pleadings, so he wrote: "No one knows for sure what 'and/or' means. Apparently those who use it have in mind making the allegation in the conjunctive and disjunctive, apparently with the idea of having an all-inclusive allegation. The object is clearly not attained. It has no place in formal legal documents such as pleading, statutes and ordinances."

The critical Trust Company official who would "put the legal profession on a plain English basis," may have met up with "and/or," and some of the less disturbing lawyer word-pets in his experience, especially with that decision which says: "'And/or' in a contract amounts in effect to a direction to those charged with construing the contract to give it such interpretation as will best accord with the situation, and for that purpose to use either 'and' or 'or' and be held down to neither."

That is enough to make out a case for our layman critic. No citations of cases are furnished, but if any one is curious enough to doubt that he really "has something," and that even lawyers may be confused by some of our own archaic phrases, let him turn to the record.

Some day this writer intends to file a court paper all in words of one syllable, which even the client may understand, and thus be led into the mistaken belief that he has hired a smart lawyer.

FEDERAL SECURITIES ACT EXEMPTIONS AND THE GENERAL PRACTITIONER

By Graham L. Sterling, Jr.*

WHETHER we have had our post-war business boom or whether it is still to come, it may be of benefit to the general practitioner to review the principal exemptions of securities offerings from registration under the Securities Act of 1933, generally known as the Federal Securities Act.

Thus, the scope of this discussion will be limited to problems under the Act which are likely to confront a lawyer with a general practice whose clients may wish to raise additional capital or perhaps dispose of a portion of their stock interest in a business, under circumstances not requiring the services of an underwriter, or where the amount involved may not justify the expense of registration.[1]

In such a case there are three exemptions from registration which may be availed of.[2] These may be designated for brevity as (1) the private offering exemption; (2) the intrastate exemption; and (3) the Regulation A exemption. While at first blush they may appear simple, each one has its pitfalls into which a lawyer not purporting to specialize in the field may fall unwittingly, with embarrassment to himself and liability to his clients.

PRIVATE OFFERING EXEMPTION

Section 4(1) of the Act exempts from the requirements of registration "transactions by an issuer not involving any public offering." The applicability of this exemption would be com-

---

*Mr. Sterling is co-author of Ballantine and Sterling's *"California Corporation Laws,"* and a member of the law firm of O'Melveny & Myers.

[1]For a comprehensive discussion of all of the exemptions under the Act, see *"Some Problems of Exemption Under the Securities Act of 1933,"* by Throop and Lane, formerly General Counsel and Assistant General Counsel of the Securities and Exchange Commission, published in IV Law and Contemporary Problems, 1, by Duke University Law School, January, 1937. This article should not be relied on, however, as coinciding in all respects with the present views of the Commission. See, also, a note entitled *"Exempted Transactions Under the Securities Act of 1933"* in 24 Washington University Law Quarterly 383 (1939).

[2]The Act also provides exemptions applicable to capital readjustments and reorganizations, which are not discussed in this article.

paratively easy if the Securities and Exchange Commission, charged with the administration of the Act, had seen fit to define such a transaction, since the Act contains no such definition. Unfortunately, the Commission has not seen fit to do so, preferring, perhaps wisely, to refrain from drawing a sharp line through a myriad of circumstances with the probable result that a particular transaction falling on the private offering side of the definition might fall on the public offering side from the standpoint of policy, or vice versa.[3]

In a letter dated April 27, 1934,[4] the Federal Trade Commission (which originally administered the Act), replying to an inquiry, stated "an offer made to not more than a small, insignificant number of persons, say twenty-five or so, would not appear to be a 'public offering,'" so long as the purchasers buy without a view to distributing the securities. One who purchases from an issuer with a view to distributing the securities is an "underwriter" as that term is used in the Act, even though not engaged in the securities business as a dealer or investment banker.[5]

This letter gave rise to a rule of thumb or practice that an offering limited to twenty-five persons who buy for investment would not be regarded as a public offering. However, in a subsequent opinion by the General Counsel of the Securities and Exchange Commission released in 1935, the earlier interpretation

---

[3]The Commission's Rule 152 states: "The phrase 'transactions by an issuer not involving any public offering' in Section 4(1) shall be deemed to apply to transactions not involving any public offering at the time of said transactions although subsequently thereto the issuer decides to make a public offering and/or files a registration statement." Although this rule is helpful in determining the applicability of various exemptions to transactions conducted *seriatim* or as a part of a single transaction, it is not helpful in determining the basic question as to what is a "public" offering.

[4]*CCH*, Federal Securities Law Service, Par. 2266.18.

[5]See definition of "underwriter" in Section 2(11) of the Act. "Distribution" as used here would appear to mean public distribution. A purchase of securities by A from an issuer, even though A intended to and did in fact buy for resale to B and C who were themselves buying for investment would seem to be a transaction not involving any public offering. "Distribution" is not defined in the Act. It has been held, however, to comprise "the entire process by which in the course of a public offering the block of securities is dispersed and ultimately comes to rest in the hands of the investing public"; *Oklahoma-Texas Trust*, 2 SEC 764, 769 (1937), aff'd 100 F. (2d) 888 (CCA, 10, 1939). See also *In the Matter of Ira Haupt & Company, cit.* Note 16 *infra*.

drawing the line between public and private offerings solely on the basis of the number of offerees was rejected, the opinion stating: "In no sense is the question to be determined exclusively by the number of prospective offerees."[6] The opinion indicates the many factors to be considered in determining the availability of the exemption, and that a definite opinion in advance, given without reference to specific facts, is impossible except in a few clear cases.

The principal factors to be considered, according to the Commission's counsel, are: (1) the number of offerees and their relationship to each other and to the issuer; (2) the number of units offered; (3) the size of the offering; and (4) the manner of offering. Underlying these factors is the fundamental point that the ultimate purchasers must be buying for investment and not with a view to distribution.

The Number of Offerees. In connection with the question of "number" it is essential to remember that it is not the number of ultimate purchasers that is material—it is the number of purchasers to whom the securities are offered that is important. "Offer" is not limited to a formal offer. Preliminary conversations to ascertain whether or not a prospect is even interested may be considered an "offer."

Furthermore, if the offerees fall into a particular class "membership in which may be determined by the application of some pre-existing standard," that is a factor which may permit an offer to a larger number than if the offerees are merely selected from the general public as likely prospects. For example, the writer understands that an offering of some $100,000,000 of bonds to approximately fifty insurance companies was regarded by the Commission as a private offering. The Commission's opinion in that case was no doubt influenced by such factors as (a) insurance companies are known to be investors rather than traders in securities, thus minimizing the possibility of public distribution; and (b) insurance companies are generally sophisticated, well-informed investors who are better able to obtain the information about the issuer necessary for an informed judgment than is the average member of the investing public.

---

[6]Securities Act Release No. 285, reported in *CCH*, Fed. Sec. Law Service at Par. 2266.17.

However, membership in a class must not be relied upon as the sole test. If the number of persons in the class is sufficiently large, an offering, while restricted to the class, may nevertheless be a public offering. For example, offerings to stockholders or to employees are likely to be regarded as public offerings unless the number of stockholders or employees is so small that the offering would be regarded as private even though not limited to such a class.[7]

Number of Units Offered. The smaller the number of units, the less chance of a public offering being involved. For example, an offering of fifty bonds of the denomination of $10,000 each, as compared with an offering of five thousand bonds of the denomination of $100 each. If the larger units, however, are exchangeable at the holders' options for units of smaller denominations, this favorable factor may be vitiated.

---

[7]See *CCH,* Pars. 2266.40, 2266.41, 2266.50-54 for opinions and cases dealing with offerings to employees and stockholders. See also *S.E.C. vs. Sunbeam Gold Mines Company, cit.* Note 16 *infra.*

Size of the Offering. In this connection the extent to which a later public offering of all or a part of the securities is likely should be considered. "* * * this exemption was intended to be applied generally to small offerings, which in their nature are less likely to be publicly offered, even if redistributed." If the securities offered are already publicly dealt in on an exchange or in an over-the-counter market, or within the reasonable contemplation of the parties are thus likely to be dealt in shortly after their issuance, these are factors which may indicate whether public distribution of the offered security in question is likely within a reasonable time.

Manner of Offering. Transactions effected by direct negotiation between the issuer and the purchaser are more likely to be non-public than those effected through the use of the machinery of public distribution. Thus, in private offerings it is the practice to have separate purchase contracts between the issuers and each purchaser, even though an investment banking firm or other third party receives compensation for finding the purchasers and negotiating some of the terms of the purchase or some of the terms of the securities, rather than to have one contract between the issuers and the investment banking firm (or other third party) whereby the latter purchases the entire offering for resale to the ultimate purchasers, or acts as the agent of the issuers in making such sales.[8]

Another consideration: Are other securities of the same class of the same issuer being offered at the same time? For example, an offering of $100,000 of stock to fifteen persons for investment might be regarded as a private offering, but the conclusion would be different if at or about the same time the issuer were to offer $100,000 of the same class of stock to the public in the same plan of financing. However, $100,000 of stock might be offered privately to fifteen persons for investment even though at the same time $100,000 of bonds were being offered privately to fifteen other persons for investment.

The availability of the private offering exemption to transactions which may be related to offerings made at or about the same time under either the intrastate exemption or the Regulation A exemption is discussed below.

---

[8]See Note 5, *supra.*

If the offering is in fact private, no filing with the Commission is required. There is no limit on the amount of the subject securities. The mails and instrumentalities of interstate commerce may be used in connection with the offering, and the offering need not be limited to residents of the state of incorporation of the issuer.

INTRASTATE EXEMPTION

Section 3(a)(11) of the Act provides that "any security which is a part of an issue sold only to purchasers resident within a single State or Territory, where the issuer of such security is a person resident and doing business within, or, if a corporation, incorporated by and doing business within, such State or Territory," is an exempt security. In this connection, it should be noted that although Section 3 of the Act in its various subsections, lists "exempt securities," it is understood to be the Commission's position that Section 3(a)(11) was intended to designate only an "exempt transaction," with the

same effect as though included in Section 4, and consequently that subsequent transactions in securities originally issued pursuant to the intrastate exemption may or may not be exempt from registration depending on the availability of an appropriate exemption for the transaction in question.

The most important elements in this exemption are: (1) the issuer must not only be incorporated by the state in question, but *also doing business in that state;* for example, an offering of securities by a California corporation to California residents would not be exempt under this section if the California corporation conducted all of its business in Arizona; (2) *each* offeree and purchaser must be a resident of the same state in which the issuer is incorporated and doing business; an offering or sale of one unit to a non-resident defeats the exemption of the entire issue, even though all other sales are made to residents;[9] (3) the purchasers must be investors, not merely under-

[9]Answering an informal inquiry, the Commission's General Counsel has indicated that in the case of an offering to California residents, a prospective purchaser which is a Delaware corporation but doing all of

writers, dealers or other persons who, though residents, purchase for resale and do resell to a non-resident; (4) the security in question must be part of an entire issue which is so sold intrastate.

The last point noted requires additional explanation. The security must be part of an entire issue which is sold intrastate. The word "issue" is another term which the law does not define and the definition of which has been carefully avoided by the Commission. Messrs. Throop and Lane in their article cited in Note 1 above appear to believe that although "issue" is usually circumscribed by the concept of "class" (*i.e.*, securities of a single class such as common stock, or preferred stock, or bonds), it is clearly not coextensive with the term "class." They conclude: "For many practical purposes, the term 'issue' approximates the term 'offering'." They also place considerable emphasis on whether or not the securities are being issued in the course of a "single plan of financing."

If the writer understands them correctly, this means that securities of the same class disposed of pursuant to a single plan of financing will almost invariably be regarded as one "issue" of securities for the purpose of determining the availability of the intrastate exemption. For example, a corporation desiring to raise $1,000,000 of additional capital cannot sell $500,000 of common stock to a non-resident institutional buyer (even though the institution were buying for investment and standing alone the transaction would be exempt as a private offering) and offer $500,000 of common stock publicly to residents of its state of incorporation under the intrastate exemption. The entire $1,000,000 of common stock would be regarded as one "issue" and the sale of a part of it to the non-resident institutional buyer would destroy the intrastate exemption as to the entire $1,000,000.

On the other hand, if under the same circumstances, the $1,000,000 were to be raised by selling $500,000 of bonds to the non-resident institution for investment and not for distribution and by offering $500,000 of common stock publicly to residents,

---

its business and having all of its properties in California will not be regarded as a California resident; but that a national banking association, which does most of its business and owns most of its properties in California, will be regarded as a California resident for such purpose.

it would seem that Messrs. Throop and Lane (although they do not expressly so state in their article) would regard these as two separate "issues" (since they are securities of different classes), with the result that the sale of the bonds would be exempt as a private offering and the sale of the stock would be exempt as an intrastate offering, even though both classes have clearly been issued "in the course of a single plan of financing." This conclusion is supported by the following statement from a later published opinion of the Commission's General Counsel, in considering the applicability of a different exemption: "Whatever may be the precise limits of the concept of 'issue' when all securities involved are of the same class, I do not believe that securities of different classes can fairly be deemed parts of a single 'issue.' "[10]

It is important, however, that the different classes of securities differ in more than name—the rights of the holder incident thereto must be actually different in substantial respects.

It is also believed that securities of a particular class may be offered under the intrastate exemption despite a previous sale of other securities of the same class to non-residents, if in fact they are separate offerings constituting distinct and unrelated financing transactions. For example, a corporation desiring to raise $500,000 of capital in 1946 and having done so by the sale of preferred stock to a few non-resident institutional investors in a manner not constituting a public offering, may, if it finds it needs additional capital in 1947, offer some of the same class of preferred stock publicly to residents of its state of incorporation pursuant to the intrastate exemption. The lapse of time is merely evidentiary. The important element is that the two offerings must actually be separate financing transactions and not merely phases of a single plan of financing.

Thus it would appear: (1) that different classes of securities of an issuer will be regarded as different "issues" for the purpose of the intrastate exemption, even though issued in connection with a single plan of financing; and (2) that different offerings of the same class of securities may, nevertheless, be regarded as different "issues" for the same purpose if the offer-

[10]Opinion of General Counsel of Commission, Securities Act Release No. 2029, August 8, 1939, *CCH*, Par. 2237.20.

ings are actually separate and distinct financing transactions—not part of a single financing plan.

The intrastate exemption is not recommended for offerings of any size, particularly through underwriters, because of the obvious risk that one sale to a non-resident, or one sale to a resident who intends to and does resell to a non-resident, will destroy the exemption of the entire issue, thus making the issuer, underwriters and dealers virtual guarantors of the value of the security at its original offering price for the period of the statute of limitations applicable in such case. This period, provided by Section 13 of the Act, would run, as to the sale to the non-resident, for a year after such sale, and, as to each other sale (whether made before or after the sale to the non-resident), for a period of one year after such other sale, but no action could be brought more than three years after the public offering.

When the exemption is used it is good practice to require each retail purchaser of the security to sign a certificate as to his residence and as to the fact that he is buying for investment and not resale. The obtaining of such certificates in good faith, although probably helpful in avoiding any criminal penalty for violating the Act, would have no such effect on the civil liability if in fact one signer of the certificate proved to be a non-resident or bought with the intention of reselling and did resell to a non-resident, nor would it deter the Commission in all probability from endeavoring to halt the distribution by application to a Federal court for an appropriate restraining order or injunction.[11]

REGULATION A EXEMPTION

Section 3(b) of the Act authorizes the Commission to exempt by regulation issues "where the aggregate amount at which such issue is offered to the public" does not exceed $300,000. Pursuant to this section the Commission has adopted various regulations[12] exempting from registration different types of offerings,

[11]For a good exposition of this exemption, see Opinion of General Counsel of Commission, Securities Act Release No. 1459 (1937), *CCH*, Par. 2245.25.

[12]For example, Regulation A-R provides a $25,000 exemption of notes and bonds secured by first liens on family dwellings; Regulation A-M provides an exemption for $100,000 of assessable shares of mining corporation; Regulation B provides exemptions relating to $100,000 offerings of fractional undivided interests in oil or gas rights; and Regulation

of which Regulation A has the broadest application and is most commonly used.[13]

Regulation A exempts securities offered to the public by an issuer providing the aggregate public offering price does not exceed $300,000 and providing further that the securities offered pursuant to this regulation in any period of one year do not exceed that amount. Offerings of outstanding securities by persons in control of the issuer may be exempted under the regulation only to the extent of $100,000 aggregate public offering price within any period of one year. The aggregate public offering price of new securities (or securities of its own issue held in its treasury) offered by the issuer and outstanding securities offered by controlling persons may not exceed $300,000 in any one year.

Certain types of securities cannot be exempted under this regulation, such, for example, as: (1) securities of investment trusts or investment companies subject to the Investment Company Act of 1940; (2) voting trust certificates; (3) certain types of oil and gas rights or certificates of interest in such rights; and (4) foreign securities.

The exemption under this regulation, contrary to some lawyers' impression, is not automatic. To obtain the exemption, a letter of notification and any prospectus or other selling material proposed to be used in connection with the offering must be filed with the appropriate regional office of the Commission for a period of at least five days, excluding Sundays and holidays, before the offering can be made. The proper regional office for issuers whose principal place of business is in Los Angeles is located at 625 Market Street, San Francisco.

The letter of notification must be filed in triplicate, including at least one signed copy. The person required to file the letter is the person by or on behalf of whom or for whose benefit the securities are to be offered. This would be the issuer in the case of authorized but unissued securities or the controlling persons in the case of an offering by them of outstanding securities.

B-T applies to $100,000 offerings of interests in an oil royalty trust, or similar trust or unincorporated association. Each of these exemptions is conditional, rather than absolute, and has its own rules which should be consulted before proceeding.

[13]Regulation A comprises Rules 220 to 224 of the Commission; *CCH*, Pars. 4220 to 4224.

No particular form is required so long as the specified information is given. However, the Commission will supply its Form S-3b-1 for this purpose if desired. The information required to be given in the letter of notification includes: (1) full names (a full name includes at least one Christian or given name, *e.g.*, "John B. Jones," *not* "J. B. Jones"), and complete mailing addresses of the issuer, its officers and directors, the person or persons by or for whom the offering is to be made, and each principal underwriter (*i.e.*, one who contracts directly with the issuer or controller with respect to participating in the distribution, as distinguished from a dealer or other person who buys from such an underwriter or otherwise contracts with such an underwriter for a participation in the offering; (2) the title of the securities; (3) the amount to be offered (*i.e.*, the number of shares or other units or principal amount of notes, bonds or other obligations); (4) the public offering price per unit; (5) the aggregate public offering price of all units; (6) the aggregate public offering prices at which any other securities of the issuer have been offered to the public within one year by the persons filing the letter; (7) the approximate proposed public offering date; (8) a list of states in which the securities are proposed to be offered; and (9) if offered by or on behalf of the issuer, the purposes for which the proceeds from the sale of the securities are to be used.

Any written communication, advertisement or radio broadcast which does more than identify the securities and state their price and by whom orders will be executed must be filed (3 copies) in the same office as the letter of notification for a like period prior to its use. Any such material must contain a prescribed statement in which the approval of the securities by the Commission, as well as any responsibility of the Commission for the accuracy or completeness of the selling material, is disavowed. Such material must also state the name of the offeror; the number of shares or other units being offered; the underwriting discount or commissions, per unit and in the aggregate (or if none, the expenses of the offering, per unit and aggregate); and, if the offering is by the issuer, the purposes for which the proceeds of the sale are to be used. Otherwise the regulation leaves the parties to their own devices as to the extent of the information contained in any such selling material.

However, the fraud sections of the Act (Sections 12 and 17) are applicable even though the securities are exempt from registration, and, as a matter of practice, the staff of the regional office will comment on the selling material filed, if they feel that it is inaccurate or incomplete or otherwise misleading. A wise practitioner will heed these comments for at least two very good reasons: First, the Commission may otherwise apply to a Federal court for an appropriate order against offering or selling the securities, and it is easier to comply with the comments than to resist such an application through available legal proceedings and, second, something that strikes the Commission's staff as inaccurate, incomplete or misleading might similarly impress a court or jury in any action brought by a purchaser of the securities to enforce the civil liability imposed by Section 12 upon one who uses the mails or instrumentalities of interstate commerce to sell a security by means of a communication which contains "an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading."

In connection with the $300,000 limitation on the aggregate public offering price of the securities, it should be noted that the Commission has regarded accrued dividends on preferred shares and accrued interest on notes, bonds or other obligations as a part of the public offering price. This may seem hypertechnical and unrealistic to a person familiar with securities offerings in which the offering price is often stated in terms of a specified sum "plus accrued dividends" or "plus accrued interest" from a particular date. In a business sense, the accrued dividends or accrued interest are not regarded as a part of the offering price (even though actually paid by the purchaser) since in the ordinary course the purchaser will receive the full dividend or interest payment at the end of the dividend or interest period in which the securities are purchased and thus the amount of the accrual will be repaid to him.

It would seem that the Commission might, by appropriate regulation, interpret Section 3(b) of the Act to exclude such accruals (particularly for limited periods such as not more than three months in the case of dividends or six months in the case of interest) from the computation of the offering price.

It should also be noted that in computing the aggregate public offering price of assessable securities under the regulation, there must be included "the aggregate amount of all assessments legally leviable thereon at the time of the offering thereof or at any time thereafter."[14] Thus it is impossible to offer fully assessable stock under the regulation.

Furthermore, if warrants or options for the purchase of securities are attached to or issued in connection with a Regulation A offering, the aggregate price payable on exercise of the warrants or options is considered a part of the offering price for the purposes of the $300,000 limitation.

In determining the applicability of the Regulation A exemption, careful attention must be paid to the question discussed above under the intrastate exemption as to whether or not the offering constitutes a single "issue." Here again there is a paucity of helpful rules and regulations or interpretations and the extent to which the various exemptions may be applicable to sales of securities made as a part of a single financing transaction is doubtful.

It would appear, for example, that the same class of securities cannot safely be offered in the same financing transaction by any attempt to make the private offering exemption, the intrastate exemption and the Regulation A exemption, or any two of them, applicable to various phases of the transaction and thus avoid registration.[15] On the other hand, different classes of

---

[14]Rule 220(f); *CCH*, Par. 4220.

[15]Reference should be made to sales to promoters who buy for investment and not for distribution whether they pay cash or contribute properties or services. These are regarded as exempt under Section 4(1) of the Act as "transactions by an issuer not involving any public offering" and will be regarded as a separate transaction for this purpose even though part of an integrated plan involving a public offering of the same class of securities, either registered or under Regulation A. Thus if the owners of an unincorporated business wish to incorporate and cause the corporation to issue stock to themselves in consideration of their transferring the business and its assets to the corporation, the issuance of such stock, assuming they acquire it without the intention of distributing it, is exempt from registration, and will be regarded as a separate transaction, even though they intend to have the corporation immediately raise additional capital by an offering of the same class of stock privately, or publicly pursuant to Regulation A or by registering the offering. See Rule 455 of the Commission (*CCH*, Par. 4455) for the definition of "promoter." However, if the promoters should be residents of a state other than the state of incorporation of the issuer, the intrastate exemption would not be available for a public offering of

securities may be sold pursuant to various exemptions, even though the sales constitute part of a single financing transaction, as: common stock, privately; preferred stock, under Regulation A; and bonds under the intrastate exemption.

However, if counsel has any doubt as to the availability of any one or more of these exemptions, he should address a letter to the Commission, either at the regional office or in Philadelphia, setting forth clearly and completely the pertinent facts and requesting the Commission's opinion on the point involved.[16]

---

the same class of securities made pursuant to the same plan of financing, since the entire issue would not have been sold intrastate. Reference should also be made to preincorporation subscriptions which are regarded as exempt transactions under Section 4(1) as transactions by a person "other than an issuer, underwriter, or dealer." However, the issuance of securities pursuant to such subscriptions is not necessarily exempt from registration depending on the availability of an appropriate exemption.

[16]See *In the Matter of Ira Haupt & Company,* Exchange Act Release No. 3845, August 21, 1946, *CCH,* Par. 75,690, in which the Commission states (emphasis supplied): "The general pattern of the Act—a sweeping prohibition, subject to a limited number of carefully defined exemptions—considered together with the nature and particularity of the

The Commission's staff handles such inquiries with promptness and courtesy and although any such opinion is not binding upon the Commission and, of course, not conclusive on any legal question involved, it will serve as a useful and practical guide on which to base advice to the client.

CONTROL SECURITIES

The general question of the applicability of the Act to sales of outstanding securities by persons in control of the issuer is too involved for the scope of this article, but there are several important points which are clear and which should be borne in mind by the general practitioner. In the first place, a sale of outstanding securities by controlling persons[17] directly to ultimate purchasers, who buy for investment and not for distribution, does not require registration. Section 4(1) of the Act exempts from registration transactions by any person other than an issuer, underwriter or dealer. A holder of outstanding securities, even though in control of the issuer, is not "an issuer, underwriter or dealer." However, the term "underwriter" is defined in Section 2(11) to include one who purchases from a controlling person or from any person under direct or indirect common control with the issuer, with a view to the distribution of the security involved. Thus one who buys control securities with a view to their resale or distribution is an underwriter and the transaction is not exempt under Section 4(1).

Therefore, when considering any proposed offering of control securities by use of the machinery of distribution, the necessity for registration must be considered to the same extent as though the offering were of authorized but unissued securities by the issuer. In other words, is the private offering

---

exemptions themselves emphasizes rather than obscures the basic purpose of the Act to protect investors and stresses the generality of its intended application. In this setting, it is clear that the *exemptions must be strictly construed and that the claimant of an exemption has the burden of showing that he falls within the terms of the exemption he claims."* Citing *S.E.C. vs. Sunbeam Gold Mines Company,* 95 F. (2d) 699 (CCA, 9, 1938).

[17]The controllers must not have acquired their securities with a view to distributing them, else they would themselves be "underwriters." "Control" means the power to direct the management, whether through ownership of securities, by contract or otherwise. It is actual control as distinguished from voting control. See Commission's Rule 455 for the definition; *CCH,* Pars. 4455 and 4455.05.

exemption applicable? If not, is the intrastate or the Regulation A exemption available? If offered under the intrastate exemption the selling stockholders, as well as the offerees, ultimate purchasers and the corporation whose securities are involved must be residents of, or if corporations, incorporated by and doing business in, the same state.[18] The Regulation A exemption, as noted above, is available only to the extent of $100,000 aggregate offering price of control securities in any one year, and the aggregate public offering price of securities offered by the issuer and control securities so offered in any year must not exceed $300,000. For example, if controlling stockholders of a corporation should offer $75,000 of their stock under this Regulation on February 1, 1947, the corporation could offer only $225,000 of its stock during the following twelve months under the same exemption.

CONCLUSION

The following points with respect to the registration exemptions discussed should perhaps be summarized for clarity and emphasis. The private offering exemption does not require any filing of any sort with the Commission and is not limited by

---

[18]The control securities need not have originally been issued intrastate providing the proposed distribution by the controller is *bona fide* and not part of a general plan of financing contemplated at the time the securities were originally issued. The doubt expressed by *Throop and Lane, supra,* Note 1, at page 111, as to the availability of the intrastate exemption for an offering of control securities unless part of an issue originally sold intrastate, does not appear to be now entertained by the Commission.

state lines or amount. The intrastate exemption likewise requires no filing with the Commission and is not limited as to amount, but is limited by state lines. However, the mails and instrumentalities of interstate commerce may be used in connection with either type of offering. The Regulation A exemption requires filing with the Commission and is limited as to amount, but the offering is not limited by state lines and the mails and instrumentalities of interstate commerce may be used.

The fraud sections of the Act (Sections 12 and 17) imposing, respectively, civil liabilities and criminal penalties, are applicable to any of the foregoing offerings of securities by the use of the mails or instrumentalities of interstate commerce, whether or not exempt from registration.

If neither the mails nor any instrumentalities of interstate commerce are used at all in connection with an offering, the Act, of course, does not apply, since its prohibitions relate only to the use of such facilities.

RULE 14—JUDICIAL COUNCIL

Notify Court of Any Settlement in Pending Cases

Failure of attorneys to observe the provisions of Rule 14 of the Judicial Council Rules of the Superior Court seems to indicate that there are a number of attorneys who do not know that this rule exists. The rule provides as follows:

> "Whenever any case pending on the trial calendar shall have been settled, the attorneys, immediately upon learning such fact, shall notify the court thereof. Failure so to do shall be deemed to be an unlawful interference with the proceedings of the court."

Not only should this rule be observed because it is a rule, but its observance will be of great assistance to the Calendar Department.

The law firm of J. A. de MARVAL, RICHELET & CO., Bartolomé Mitre 559, Buenos Aires, Argentina, S. A., has offered to mail without charge to attorneys representing clients having business in Argentina, a digest of corporation and other pertinent laws of that country. If you are interested apply directly to the above firm.